No. 96-1578

In The

Supreme Court of the United States

October Term, 1996

HON. THOMAS R. PHILLIPS, HON. RAUL A. GONZALEZ, HON. JACK HIGHTOWER, HON. NATHAN L. HECHT, HON. LLOYD DOGGETT, HON. JOHN CORNYN, HON. BOB GAMMAGE, HON. CRAIG T. ENOCH, HON. ROSE SPECTOR, TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION, AND W. FRANK NEWTON, IN HIS OFFICIAL CAPACITY AS CHAIRMAN OF THE TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION,

Petitioners,

v.

WASHINGTON LEGAL FOUNDATION, WILLIAM R. SUMMERS, AND MICHAEL J. MAZZONE,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF OF AMICUS CURIAE AMERICAN BAR ASSOCIATION IN SUPPORT OF PETITIONERS

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INTEREST OF AMICUS CURIAE[1]

The American Bar Association ("ABA") is a voluntary membership organization of the legal profession dedicated to the promotion of a fair and effective system for the administration of justice. Its membership includes approximately 342,000 lawyers.

The ABA has supported the creation of IOLTA (Interest on Lawyer's Trust Accounts) programs in every state and in the District of Columbia for almost two decades. It views IOLTA as an integral component in the funding of civil legal services to the indigent. The ABA formed an Advisory Board and Task Force on IOLTA in 1981. Two years later the ABA Board of Governors officially approved state-authorized IOLTA programs. Meanwhile, the ABA Standing Committee on Ethics and Professional Responsibility reviewed the ethical implications of IOLTA programs and concluded that participation in state-authorized IOLTA programs was consistent with lawyers' professional and ethical responsibilities. The ABA has continued to support the adoption of IOLTA programs in every state, and in 1988, the ABA House of Delegates specifically resolved to encourage states to adopt or convert to mandatory IOLTA programs.

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[1] The parties have consented to the submission of this brief. Their letters of consent have been filed with the Clerk of this Court. Neither this brief nor the decision to file it should be interpreted to reflect the views of any judicial member of the American Bar Association. No inference should be drawn that any member of the Judicial Division Council has participated in the adoption of or endorsement of the positions in this brief. This brief was not circulated to any member of the Judicial Division Council prior to filing.

The net income collected through each IOLTA program is distributed as grants. According to a survey conducted by the ABA Commission on IOLTA, approximately 90 percent of IOLTA grants in the United States support either the provision of direct civil legal services or pro bono legal services to the poor. Some IOLTA grants fund programs related to the administration of justice, such as alternative dispute resolution programs, young lawyer special public service projects, victim services programs, court-appointed special advocate programs, and *pro se* litigation programs. In addition, some IOLTA grants are provided for legal education and loans and scholarships for law students.

IOLTA programs are a critical part of the indigent civil legal services delivery system in the United States and have become even more critical after the budget of Legal Services Corporation, the entity providing federal funding for legal services to the poor, was reduced by 30 percent. A survey conducted in 1992 by Justice Howard Dana of the Maine Supreme Court found that IOLTA funds provided approximately 25 percent of all funding for staffed legal services programs. Between 1983 and 1993, according to a Legal Services Corporation survey, IOLTA programs contributed $405.8 million to Legal Services Corporation-funded programs. In addition, according to a survey conducted by the ABA Center for Pro Bono in 1991, IOLTA programs fund approximately 26 percent of the budgets for bar association-sponsored pro bono programs. Today, IOLTA programs represent the second largest funding source for the delivery of civil legal services to the poor in this country. The ABA is strongly committed to ensuring that all people in this

country receive needed legal services and have access to the nation's civil justice system. Therefore, the ABA has a significant interest in the future availability and effectiveness of IOLTA programs.[2]

In addition, the ABA operates a Commission on IOLTA and an IOLTA Clearinghouse which monitor and provide information about the operation of IOLTA programs across the country. The ABA is therefore uniquely qualified to provide this Court with a full understanding of IOLTA programs in Texas and throughout the nation.

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[2] Two of the twelve goals that the ABA has adopted reflect its interest in ensuring the availability and effectiveness of IOLTA programs: Goal I – To promote improvements in the American system of justice; Goal II – To promote meaningful access to legal representation and the American system of justice for all persons regardless of their economic or social condition.

STATEMENT

The National Conference of Chief Justices endorsed and encouraged the development and implementation of IOLTA programs by resolution in February 1979. IOLTA-type programs were first implemented in Australia in the 1960s, and soon spread to Canada, New Zealand, and several African countries. All fifty states, either through the state's highest court or the state legislature have approved IOLTA programs, as has the highest court of the District of Columbia. Fifty of these programs are in operation.[3] In this country, the programs are premised on specific banking laws and regulations that do not permit many client deposits with lawyers to earn income, but do permit banks to pay interest if those same deposits are structured as an IOLTA account.

There are essentially two types of situations in which clients deposit funds with lawyers. One is when a client finds it convenient to have an attorney hold funds for generally short periods of time in connection with specific legal undertakings. For example, clients often deposit real estate closing costs with their lawyers a day or two before the closing is scheduled. Clients also may arrange for settlement proceeds to be paid to their lawyers who then transfer the proceeds to their clients by check. Buyers and sellers of real property also frequently arrange to have the seller's lawyer, rather than the seller

[3] An IOLTA program has been approved in concept by the Supreme Court of the last remaining state, Indiana, but the program is not yet operational. Of the programs currently in operation, 27 are mandatory, 20 permit attorneys to affirmatively opt out of the program, and 3 are voluntary. *See* attached Appendix.

or other agent, hold the buyer's earnest money deposit between offer and closing. The other type of situation in which clients deposit funds with lawyers is to satisfy a lawyer's request for advance payment as part of their business arrangement, such as refundable retainers or pre-payments of court and litigation expenses.

Traditionally, most lawyers placed these client deposits in a pooled demand account separate from their own funds.[4] The funds were therefore available on demand when the client needed them but did not, under the banking laws applicable in most states before 1980, earn interest. The banking institutions had full use of these funds while they were deposited and retained all income derived from that use.[5]

[4] Separation of client funds from the lawyer's own funds has been imposed by most states as an ethical requirement. *See, e.g.*, ABA Model Rules of Professional Conduct ["ABA MRPC"] R.1.15 (1997).

[5] An exception was possible in the relatively unusual situation in which a client did not need immediate access to the funds and the amount of money was large enough or length of time was long enough to generate more interest than needed to cover administrative costs. With the client's agreement, the lawyer could place these funds in a savings or time account which did pay interest but did not guarantee immediate access. *See* ABA Comm. on Ethics and Professional Responsibility, Formal Op. 348, 688 A.B.A.J. 1503 (1982) ["ABA Formal Op. 348"]. Under these circumstances, clients would have to bear additional costs for services rendered by the bank or the lawyer in accounting for the interest, remitting it to the client, and generating tax forms for both the client and the Internal Revenue Service. Lawyers are not permitted to deduct these costs from the interest generated, *see id.*, but they are permitted to bill clients for reasonable administrative expenses. *See Carroll*

In 1980, Congress passed the Consumer Checking Account Equity Act, codified at 12 U.S.C. § 1832, which for the first time permitted banks throughout the country to pay interest on certain demand accounts. These accounts became known as Negotiable Order of Withdrawal or NOW accounts. Under the statute, NOW accounts are available only to one or more individuals, government agencies, and non-profit philanthropic, religious, educational or political organizations. *See* 12 U.S.C. § 1832(a)(2); 12 C.F.R. § 204.130. Demand accounts for corporations, partnerships, associations, insurance companies, and the like, continue to pay no interest.

Funds deposited by a fiduciary, such as a lawyer, may be placed in a NOW account only if the beneficiaries are themselves eligible to maintain NOW accounts. *See* 12 C.F.R. § 204.130(e). Likewise, escrow accounts may be held as NOW accounts only "if the entire beneficial interest is held by individuals or other entities eligible to maintain NOW accounts directly." 12 C.F.R. § 204.130(b)(2). Thus, a lawyer is permitted by federal banking law to place client funds in a NOW account only if the client is an individual, a governmental unit, or a non-profit philanthropic, religious, educational or political organization. As a result, although NOW accounts may provide a useful vehicle in some cases, deposits from clients that are corporations, partnerships, associations, insurance companies and the like, are not, by themselves, eligible.

Further, bank charges are deducted from the funds available in NOW accounts so that most deposits even for

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v. State Bar of California, 166 Cal. App. 3d 1193, 1205, 213 Cal. Rptr. 305, 312 (4th Dist.), *cert. denied*, 474 U.S. 848 (1985).

clients who are eligible for these accounts would fail to earn any income. Thus, as before, in most cases banks alone would enjoy the beneficial use of client deposits.

IOLTA was developed as a method to use the new banking laws to wrest some of this beneficial use away from the banks and, where it was not possible to confer it on the client, use it to fund legal services for the poor and equal access to justice programs.[6] IOLTA programs take advantage of the provision that permits a non-profit philanthropic organization to maintain a NOW account. Under an IOLTA program, each lawyer or law firm establishes a NOW account for which the interest, less bank charges, is paid to the state's IOLTA organization. Client deposits are pooled in the account, reducing bank charges and generating more net interest. Moreover, because all charges are paid by and all interest is paid to one entity, no costs are incurred for attributing interest or charges to particular clients.[7] Finally, although NOW accounts in which clients are the beneficiaries are limited to deposits from individuals, governmental units or qualifying non-profit organizations, deposits from every type of client

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[6] In this country, certain bar associations had shown interest in IOLTA programs as early as the 1970s, when NOW accounts were approved for operation in a few states and the Federal Reserve Board of Governors recommended to Congress that such accounts be made available nationally. *See In re Interest on Trust Accounts*, 356 So. 2d 799 (Fla. 1978).

[7] Neither lawyer nor bank needs to attribute interest or charges to specific deposits because the IOLTA organization receives all interest less all charges. Neither lawyer nor bank needs to generate and send tax forms to each client because the clients exercise no control over the distribution of income from the account. *See* Rev. Rul. 87-2, 1987-1 C.B. 18; Rev. Rul. 81-209, 1981-2 C.B. 16.

may be placed in an IOLTA account because the sole beneficiary of the income generated by an IOLTA account is a qualifying non-profit organization.[8]

Nonetheless, although all client deposits are eligible to be placed in an IOLTA account under federal banking laws, not all client deposits are eligible to be placed in an IOLTA account under IOLTA rules. Lawyers are required to make a determination whether the client deposit is capable of earning income for the client. In making that determination, the lawyer must consider the amount to be deposited, the length of time it will be held, the likely bank charges, and the likely administrative costs of establishing, maintaining, and complying with tax requirements. Any client funds that can earn more interest in a non-IOLTA account than will be consumed by administrative costs may not be placed in an IOLTA account.[9]

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[8] IOLTA organizations are either bar foundations, independent 26 U.S.C. § 501(c)(3) organizations created to administer IOLTA, or extensions or special programs of the state, state supreme court or state bar.

[9] In Texas, and a number of other states, lawyers also consider whether the client's deposit could earn more interest if aggregated with other NOW-eligible client deposits in an aggregated account than will be consumed by administrative costs. "If the client funds deposited in an individual or pooled account *can* earn interest above and beyond such costs and charges, and thus, earn a net return to the client in *any* amount, the funds may not be deposited into an IOLTA account." Justices of the Supreme Court of Texas Suggestion of the Appropriateness of a Rehearing En Banc, *WLF v. TEAJF*, No. 95-50160, br. at 6 (5th Cir. Sept. 25, 1996) (explaining the rules governing the Texas IOLTA program challenged here). The Supreme Court of Texas created the Texas IOLTA program and promulgated the rules governing it, *see* Texas Rules of Court – State, Rules Governing

IOLTA programs were structured to divert income legally from banks to legal services and equal access to justice programs. They were not intended to, and under their rules may not, divert income that could otherwise be earned by a client.[10]

No court had ever struck down an IOLTA program on constitutional grounds before the decision below. To the contrary, every other court that has considered the question has rejected arguments that IOLTA programs contain any constitutional infirmities. *See, e.g., Cone v. State Bar of Florida*, 819 F.2d 1002 (11th Cir.), *cert. denied*, 484 U.S. 917 (1987); *Washington Legal Found. v. Massachusetts Bar Found.*, 993 F.2d 962 (1st Cir. 1993); *Petition of Mass. Bar Ass'n*, 478 N.E.2d 715 (Mass. 1985); *Carroll v. State Bar of California*, 166 Cal. App. 3d 1193, 213 Cal. Rptr. 305 (4th Dist.), *cert. denied*, 474 U.S. 848 (1985); *Petition of N.H. Bar Ass'n*, 453 A.2d 1258 (N.H. 1982); *Petition of Minn. State Bar Ass'n*, 332 N.W.2d 151 (Minn. 1982); and *Matter of Interest on Trust Accounts*, 402 So. 2d 389 (Fla. 1981).

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the Operation of the Texas Equal Access to Justice Program (West 1996). The additional precaution appears, however, to have little practical application. First, only deposits from individuals or other qualifying clients may be aggregated in a non-IOLTA NOW account. Second, aggregated accounts impose very high administrative costs in addition to the types of costs imposed by individual accounts, because it is necessary to attribute the appropriate proportion of interest and charges to each client and to send individual 1099-INT tax forms for each client to both the client and the Internal Revenue Service.

[10] In Texas, for example, if a lawyer deposits funds in an IOLTA account that do not qualify under these rules, a mechanism exists for reimbursing the client.

SUMMARY OF ARGUMENT

That client funds placed in IOLTA accounts do not earn income for the clients is not the fault of the IOLTA rules; it is the result of the nature of the deposits, the banking laws, and the tax laws. Absent an IOLTA program, these funds would still not generate income for these clients. Indeed, client deposits capable of generating income for the clients are not permitted by state law to be placed in an IOLTA account. Thus, these clients have no legitimate claim of entitlement to income on their deposits under the prevailing law and contractual understandings unrelated to IOLTA programs, and therefore they do not meet the standard required to establish a property interest cognizable under the Fifth Amendment. Pt. IA.

The interest generated on IOLTA accounts does not result from interference with any property rights the clients have in the funds deposited. Therefore, clients cannot premise a claim to IOLTA interest on a right to exclude others from using those funds. Pt. IB.

Neither *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155 (1980), nor the Texas decision the Fifth Circuit relied on, establish a legitimate claim of entitlement here. Both considered the existence of a property right in interest under the very different circumstances of deposits that would have generated the same income if deposited by their owners. Pt. IIA. The existence or nonexistence of a property right turns on just such distinctions in background law as this Court has repeatedly found. *See, e.g., United States v. Willow River Power Co.*, 324 U.S. 499 (1945). Pt. IIB.

Likewise, the fact that an IOLTA account generates interest does not confer a property right to that interest on clients who – wholly apart from the challenged IOLTA rules – are legally or practically incapable of earning interest directly. Clients who have no right to NOW account interest income under the banking laws, or under the bank's contractual terms, do not gain the right to NOW interest income generated in the name of entities subject to different rules. The right to property that comes into existence pursuant to particular laws remains subject to the conditions imposed by those laws. *See, e.g., Dames & Moore v. Regan*, 453 U.S. 654 (1981). Pt. IIC.

The decision below therefore should be reversed.

ARGUMENT

I. CLIENTS HAVE NO CONSTITUTIONALLY COGNIZABLE PROPERTY INTEREST IN THE INCOME GENERATED BY IOLTA ACCOUNTS.

A. Clients Have No Legitimate Claim Of Entitlement To Interest On IOLTA Deposits.

It is long settled that a constitutionally cognizable property interest exists only where there is "a legitimate claim of entitlement . . . as defined by existing rules or understandings that stem from an independent source." *Board of Regents of State Colleges v. Roth*, 408 U.S. 564, 577 (1972).[11] That independent source may be state law, *id.*, or

[11] Although initially recognized in the context of procedural due process, the test has long been applied in

federal law. *See, e.g., Atkins v. Parker*, 472 U.S. 115 (1985); *Dames & Moore*, 453 U.S. at 674 n.6.

The existing rules and understandings applicable to client deposits in IOLTA accounts make clear that the clients have no "legitimate claim of entitlement" to interest on these deposits. First, many of these clients are prohibited by the banking laws from earning interest on demand accounts because they are not individuals, governmental units, or qualifying non-profit organizations. Second, the deposits placed in IOLTA accounts from clients who do qualify for NOW accounts are not large enough or held for long enough to actually earn any income under the express contractual terms available from the banks. If they were, IOLTA rules in every jurisdiction require the deposits to be placed in a non-IOLTA account.

Thus, nothing is taken from clients and no opportunity to earn income is diverted. Had the clients kept control of their funds and attempted to earn interest income from a bank for the applicable time period by any means available under the law, they would not have been able to do so.[12] In other words, these clients would earn no income on their nominal or short-term deposits

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Takings Clause decisions. *See, e.g., Ruckelshaus v. Monsanto Co.*, 467 U.S. 986, 1001 (1984); *Webb's Fabulous Pharmacies*, 449 U.S. at 160-61.

[12] If a client eligible for a NOW account deposited his funds into an individual account, at best the client might be able to withdraw the same amount originally deposited when the funds were needed. In most cases, the client could not do even that because part of the original deposit would have been applied to pay bank charges.

whether or not Texas had mandated the IOLTA program. *Accord Cone*, 819 F.2d at 1006. They have no basis therefore in law or mutual understandings on which to stake a legitimate claim of entitlement to the interest income generated when their deposits are placed in an IOLTA account.

B. Clients And Lawyers Have No Legitimate Claim Of Entitlement To IOLTA Interest On Any Other Basis.

Clients also cannot premise a claim to IOLTA interest on a right to control how their funds are used. Whatever constitutionally cognizable right they may have had to exclude others from using these funds was voluntarily relinquished when they deposited the funds with a lawyer.

Nothing in the IOLTA rules or any other law requires any client to deposit money with any lawyer. For example, clients who deposit real estate closing payments with lawyers do so for their own convenience. They are completely free instead to bring their real estate closing payments to the closing itself. Likewise, clients who agree to settlement terms providing for the settlement payments to be collected and distributed by their attorneys do so because it is a mutually acceptable solution to a practical problem. No law requires clients to agree to such terms. They remain free to require that settlement payments be sent directly to them. IOLTA rules and other laws also do not require clients to deposit real estate escrows with an attorney. The choice to use an attorney to hold a real

estate escrow payment rather than the seller or a different third party is made by the parties to the sale.

Similarly, cost advances and refundable retainers are deposited pursuant to the terms of the contract between the lawyer and the client. There may be lawyers who are unwilling to negotiate these terms but that is a choice made by the lawyer, not the state. No client is ever under an obligation to deposit cost or fee advances with a lawyer unless the client voluntarily undertakes to do so.

In other words, clients who deposit funds with their lawyers are in no worse a position than partnerships who deposit money in a bank checking account.[13] Banks are prohibited by federal law from paying interest on a partnership's checking accounts, even though the funds deposited are used to earn income for the bank. *See* 12 U.S.C. § 1832(a)(2). But once the funds are deposited, the bank is free to use them in any way permitted by law without regard for the partnership's views, so long as it provides the principal on demand. Thus, the bank may invest the funds in ways the partnership thinks improvident. And the bank may loan the funds to an endeavor to which the partners are ideologically and morally opposed.

Such activities have never been thought to implicate constitutional rights because the partnership's inability to control the bank's use of its deposit is not the result of a

[13] The client is actually in a better position than the partnership because if the client's deposit is capable of earning income while deposited, it cannot be placed in an IOLTA account.

governmental encroachment on its property rights. The partnership's inability to control the bank's use of its deposit is the result of the partnership's decision to deposit the money with the bank. However convenient a checking account may be, and however non-negotiable the terms offered by the bank, opening the checking account is in no way mandatory. The same is true of a client's inability to prevent its lawyer from placing nominal or short-term deposits in an IOLTA account. Although it may be convenient to deposit certain funds with the lawyer, and the terms for depositing advances may not be particularly open to negotiation, the client who wishes to exercise a right to exclude remains free to make different arrangements. Thus, the IOLTA program does not contravene any right the client may have over how its funds are used.[14]

[14] Moreover, lawyers required to establish and use IOLTA accounts certainly have no property interest in any IOLTA interest generated because they have no legitimate claim of entitlement to either the funds themselves or to any income generated from the funds. Indeed, lawyers who hold client funds are prohibited from using these funds for their own benefit or even commingling the funds with their own. *See, e.g.*, ABA MRPC Rule 1.15; *see also* ABA/BNA Lawyers' Manual on Professional Conduct 45:109-45:111 (1997). Further, when interest is earned on such funds, lawyers are also forbidden to treat that interest as their own. They are not permitted, for example, to deduct legitimate charges from that interest, even when the charges are for administrative costs incurred in servicing the account or reporting the interest. *See* ABA Formal Op. 348. As discussed *supra* note 5, however, lawyers are permitted to recoup the cost of handling such accounts through normal billing.

II. THE "INTEREST FOLLOWS PRINCIPAL" RULE APPLIED IN INTERPLEADER CASES IS IRRELEVANT TO THESE QUITE DIFFERENT CIRCUMSTANCES.

In concluding that these clients had a property interest in the interest generated by IOLTA accounts, the court below relied on two inapposite decisions: this Court's *Webb's Fabulous Pharmacies*, 449 U.S. 155, and the Supreme Court of Texas' *Sellers v. Harris County*, 483 S.W.2d 242 (Tex. 1972). Both cases determined the ownership of interest on interpleaded funds, which in every relevant sense is wholly unlike the interest at issue here.

A. Interpleaded Funds Differ From IOLTA Accounts In Three Critical Ways.

First, in both *Webb's Fabulous Pharmacies* and *Sellers*, the interpleader was required by state law to deposit the principal in order to avail itself of statutory protection from suit. And, in both instances, the state did not permit the owners of the funds to have access to them until the conclusion of lengthy court proceedings.[15] In *Webb's Fabulous Pharmacies*, the principal was the sale price of a company all of which was claimed by the company's creditors. In *Sellers*, the principal was insurance proceeds that were owed to one of two adverse claimants.

In contrast, the principal in the instant case is composed entirely of client funds that the clients are free to retain and invest themselves but have chosen instead to

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[15] *See, e.g., Webb's Fabulous Pharmacies*, 449 U.S. at 164.

deposit with their lawyers, for their own or their lawyers' convenience. Nothing in the IOLTA rules, or any law, requires the clients to make this choice.

Second, in both *Webb's Fabulous Pharmacies* and *Sellers* the funds were of sufficient size, and deposited for a sufficient length of time, to earn net income above and beyond the cost of administering the deposits. In *Webb's Fabulous Pharmacies*, as this Court emphasized, the deposit earned $90,000, none of which was needed to cover administrative costs because those costs had already been deducted from the principal. 449 U.S. at 158. Similarly, in *Sellers*, the single deposit at issue was earning $6,000 each month it was held. 483 S.W.2d at 242. *Sellers* rejected the county's claim to all of that interest because the amount was "not reasonably related to the value of the county's services in safeguarding and investing the principal." 483 S.W.2d at 244.

The opposite is true of the interest at issue here. Because the IOLTA program is only lawfully available for client deposits that are not capable of earning interest in excess of administrative costs, the individual deposits in IOLTA accounts are not capable of earning *any* interest in excess of administrative costs for their owners.

Third, in both cases the only infirmity preventing the owners of the principal from investing the funds themselves was the delay imposed by the course of litigation. There is no indication in either decision that the owners could not themselves have placed the funds in identical accounts in their own names, if the funds were in their possession. The same is certainly not true for many clients whose deposits are placed in NOW accounts under

the IOLTA program. As discussed above, although most client deposits are needed quickly and therefore must be placed in demand accounts, demand accounts that pay interest are not available to corporations, most companies, partnerships, and many associations.

B. Contrary To The Fifth Circuit's View, Such Differences Are Critical To The Constitutional Analysis.

The existence or non-existence of a property interest turns on just such distinctions, as this Court has long recognized. This Court, for example, has found that the existence of a property owner's interest in the natural level of a stream turns on whether the stream is navigable. Thus, an interest in the natural flow-off of water in a non-navigable stream is a property interest protected by law, *see United States v. Cress*, 243 U.S. 316, 330 (1917), and an interest in the natural flow-off of water in a navigable stream is not, *see Willow River Power*, 324 U.S. at 511. Similarly, whether a teacher has a property interest in a renewed employment contract depends on the express terms of the existing contract, the employer's rules and policies, and the employer's practices. *See Perry v. Sinderman*, 408 U.S. 593, 601-02 (1971). A teacher's property interest in a renewed employment contract is therefore hinged on every change in an employer's rules, policies, or practices.

The Fifth Circuit's dismissal of such distinctions as too "fickle" a basis for determining the existence of a property right, Pet. App. 16a n.47 & 8a, is wholly at odds

with this Court's jurisprudence. This Court has consistently recognized that the existence of a property interest rests on just such particular and changeable factors. Property right claims require an inquiry into the laws, rules, express and implied contractual understandings that define the legitimacy of the claim, even though contracts and mutual understandings are often specific to the parties, and even though governing laws can be expected to change "from time to time, by various measures newly enacted by the State," especially with respect to personal property "by reason of the State's traditionally high degree of control over commercial dealings." *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1027-28 (1992).

Indeed, the Fifth Circuit's extraction of a widely applicable general rule, "interest follows principal," from *Webb's Fabulous Pharmacies* and *Sellers*, Pet. App. 8a, 10a, is inconsistent even with those decisions. Neither purported to determine the existence of a constitutionally cognizable property right in interest under all circumstances. This Court emphasized the narrowness of its holding in *Webb's Fabulous Pharmacies*, limiting it to circumstances where deposit of the funds is required by state statute and where the administrative cost of handling the deposits has been paid separately. 449 U.S. at 164. Moreover, the Court expressly reserved judgment even with respect to interpleader interest under different circumstances, explaining:

> We express no view as to the constitutionality of a statute that prescribes a county's retention of interest earned, where the interest would be the only return to the county for services it renders.

Id. at 165. Similarly, *Sellers'* finding of a property right was premised on the fact that more interest was generated than necessary to cover administrative costs. 483 S.W.2d at 243-44. The court therefore reinstated the trial court's judgment that the claimants had a right to the interest less a reasonable fee for administrative services. 483 S.W.2d at 244.[16]

The Fifth Circuit's reliance on these decisions to find a property interest attaching to accrued interest, regardless of whether it exceeds administrative costs, Pet. App. 13a, is unsupportable. *Webb's Fabulous Pharmacies* and *Sellers* applied the axiom "interest follows principal" not only where net interest existed but expressly *because* net interest existed. As other courts have noted:

> when Justice Johnson observed in *Himely v. Rose* that 'interest goes with the principle, as the fruit with the tree,' his illustration necessarly assumed the existence of a fruit-bearing tree.

Cone, 819 F.2d at 1004 (quotations and citations omitted). Where, as here, the tree is incapable of bearing fruit for the owners of the deposits, those owners have no legitimate claim of entitlement to any fruit.[17]

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[16] *See also Harris County v. Sellers*, 468 S.W.2d 950, 954 (Tex. Civ. App. 1st Dist. 1971) (describing trial court's decision), *rev'd*, 483 S.W.2d 242 (Tex. 1972).

[17] That these clients do not have the property interest asserted is underscored by considering how the Takings Clause would apply. The Takings Clause requires the government, when taking private property for public use, to pay "just compensation." U.S. Const. amend. V. Where, as here, the claimants have suffered neither actual losses nor lost opportunity costs, "just compensation" would presumably be $0, and the Takings Clause would not be implicated.

C. The Fact That An IOLTA Account Is Able To Earn Interest Does Not Confer A Property Right The Clients Otherwise Would Not Have.

The court below further misapplied *Webb's Fabulous Pharmacies* in concluding that, although Texas had no obligation to generate interest on client deposits, once the IOLTA program does, the interest belongs to the clients. This Court's recognition in *Webb's Fabulous Pharmacies* that the owners of an interpleaded deposit were entitled to net interest generated, even though the state was not obligated to place the deposit in an interest-bearing account, presupposed that the owners themselves could have made the same investment. In other words, the owners were entitled to the proceeds from the investment they could have made had they been permitted to take possession of the funds as early as they had a legitimate claim of entitlement to them.

The Fifth Circuit's decision at issue here, in contrast, is that the owners of funds who choose not to invest them are entitled to proceeds from an investment they are not entitled to make. That proposition finds no basis in *Webb's Fabulous Pharmacies* or in any other decision of this Court. Indeed, in *Dames & Moore*, this Court rejected an analogous argument. Dames & Moore, which had obtained an attachment on property of certain Iranian banks, challenged President Carter's revocation of licenses to obtain attachments of Iranian assets and nullification of all non-Iranian interests in such assets. 453

U.S. at 663. This Court rejected the company's argument that, although the President could have forbidden attachments, "once he allowed them the President permitted claimants to acquire property interests in their attachments." *Id.* at 674 n.6. This Court found that the only property right Dames & Moore acquired was limited by the President's ability to nullify it, and the fact that Dames & Moore had been permitted to obtain an attachment did not change Dames & Moore's position. *Id.*

Here, the existence of interest cannot change these clients' positions any more than the existence of an attachment changed Dames & Moore's position. These clients had no property right in interest on the funds if deposited in their own names – unlike the claimants in *Webb's Fabulous Pharmacies* – and continue to have no property right to interest on the funds. That some interest can be generated for a different entity altogether under prevailing laws and contractual understandings does not affect the legitimacy of these clients' claims to entitlement.

The Fifth Circuit's opposite rule cannot be correct, as is made even more clear by considering the dilemma of implementing it. Deposits from all types of clients are deposited in IOLTA accounts. Because the proceeds go to an IOLTA organization, deposits from many clients who are not themselves eligible for NOW accounts may be included. If, however, the interest belongs to these clients, the bank has violated federal law by opening the account in the first place and by paying the interest. Thus, the very interest that creates the clients' property interest, according to the Fifth Circuit, cannot lawfully exist under the court's reading.

Furthermore, wholly apart from that problem, the Fifth Circuit's conclusion that these clients have a property right to the interest triggers a series of practical and legal obligations. Both interest and charges must be apportioned among those clients whose deposits have been placed in the account and various tax reporting rules must be complied with. However, the bank charges, or lawyer's fee, for providing these subaccounting services, given the nominal amount or short duration of the deposits, can be expected to be larger than the interest generated by the account.[18] As a result, in most if not all cases, the accrued interest and probably some of the principal will be required to cover the charges.

Application of the Fifth Circuit's finding of a property right to the interest on IOLTA accounts, if IOLTA rules are deemed a taking, will almost certainly provide no interest to these clients, and will likely cost them part of their principal – an amount that is fully protected and

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[18] As explained *supra*, the reason client deposits placed in IOLTA accounts earn sufficient interest to offset costs is because all of the interest and charges are aggregated and designated for the non-profit IOLTA entity. If, instead, the interest and charges have to be apportioned among the clients with funds held in the IOLTA account, the charges will most likely equal or exceed the amount of interest accruing to each client. This effect is illustrated by the claim at issue in *Cone*, 819 F.2d 1002. The client's nominal deposit of $13.75 would have earned $.06 per month in gross interest. The bank charged $2.00 per month for each subaccount in a pooled account, plus $.25 per transaction. *Id.* at 1006 n.6. Recognition of such a client's property right to the interest in an IOLTA account would have cost the client $1.94 of principal each month, assuming no transactions and no additional bank charges.

available on demand under the IOLTA rules. The actual value of the property interest recognized by the Fifth Circuit, even if it could exist lawfully, which it cannot, basically ranges between zero and a net loss.

In sum, under prevailing law and contractual understandings, *this* property right and *this* interest cannot coexist. The generation of income from these accounts is *contingent* on the clients having no interest in it. If they do, the disputed property ceases to exist.

It is a conundrum easily avoided by recognizing that the question of what property interest, if any, these clients have must be answered by reference to the client's legitimate claims of entitlement to the interest, and not by reference to the legitimate claims of any other persons or entities. Thus, the banks' ability to use client deposits to earn income before the banking laws were changed and IOLTA programs were instituted did not, and cannot, confer a property interest on the clients in that income. Likewise, an IOLTA organization's ability to use client deposits to earn income also cannot confer a property interest on the clients in that income. The only claims to income on their deposits that these clients may legitimately assert must be grounded in the prevailing law and contractual understandings, apart from IOLTA rules, that affect them.

For most clients, the change in the banking laws in 1980 had no effect on their right to income from deposits. And, under IOLTA rules, these are the only clients whose deposits may be placed in IOLTA accounts. Thus, the clients whose deposits are placed in IOLTA accounts stand in the same position as before. The existence of

interest under the IOLTA system, like the existence of income from the deposits under the traditional system, does not affect the calculus for assessing their claims of entitlement.

CONCLUSION

For the foregoing reasons, this Court should reverse the decision of the court of appeals below.

Respectfully submitted,

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APPENDIX

Listed below is the citation of the authorizing legislation or court rule for each of the 50 operational IOLTA programs in the United States.

Alabama:	Alabama Rules of Professional Conduct, Rule 1.15 (1992)
Alaska:	Alaska Rules of Professional Conduct, Rule 1.15(d) (1989)
Arizona:	Code of Professional Responsibility, DR 9-102; Rules of the Arizona Supreme Court, Rule 29(a) (1984)
Arkansas:	Arkansas Model Rules of Professional Conduct, Rule 1.15 (1994)
California:	CAL. BUS. & PROF. CODE § 6210-6228 of Article 14, Chapter 4 (1981)
Colorado:	Colorado Rules of Professional Conduct, Rule 1.15 (1992)
Connecticut:	CONN. GEN. STAT. § 51-81(c) (1993); Connecticut Rules of Professional Conduct, Rule 1.15 (1993)
Delaware:	Delaware Lawyers' Code of Professional Responsibility, DR 9-102 (1983)
D.C.:	District of Columbia Court of Appeals Rules Governing the Bar, Rule 10, Appendix B (1985)
Florida:	Rules Regulating the Florida Bar, Rule 5-1.1(d) (1989)
Georgia:	Rules and Regulations for the Organization and Government of the State Bar of

	Georgia, Rule 4-102(d), Standard 65; Georgia Code of Professional Responsibility, DR 9-102(c), Rule 3-109 (1989)
Hawaii:	Rules of the Hawaii Supreme Court, Rule 11 (1991)
Idaho:	Idaho Rules of Professional Conduct, Rule 1.15 (1989)
Illinois:	Illinois Rules of Professional Conduct of the Rules of the Supreme Court of Illinois, Article 8, Rule 1.15 (1987)
Iowa:	Iowa Code of Professional Responsibility, DR 9-103 (1985)
Kansas:	Kansas Model Rules of Professional Conduct, Rule 1.15 (1992)
Kentucky:	Kentucky Supreme Court Rule 3.830 (1991)
Louisiana:	Louisiana Rules of Professional Conduct, Rule 1.15 (1995)
Maine:	Maine Bar Rules, Rules 3.6(e)(4), (5) (1993)
Maryland:	MD. CODE ANN. BUS. OCC. & PROF., § 10-303 (1995)
MA.:	Massachusetts Supreme Judicial Court Rule 3:07; Code of Professional Responsibility, DR 9-102 (1990)
Michigan:	Michigan Rules of Professional Conduct, Rule 1.15 (1990)
Minnesota:	Minnesota Rules of Professional Conduct, Rule 1.15(d) (1993)
Mississippi:	Mississippi Rules of Professional Conduct, Rule 1.15 (1993)
Montana:	Montana Rules of Professional Conduct, Rule 1.15 and Rule 1.18 (1996)

Nebraska:	Nebraska Code of Professional Responsibility, DR 9-102 (1984)
Nevada:	NEV. REV. STAT. §§ 217-221 (1992)
New Hampshire:	New Hampshire Supreme Court Rules 50 and 50-A (1991)
New Jersey:	New Jersey Supreme Court Rule 1:28A (1988)
New Mexico:	New Mexico Rules of Professional Conduct, Rule 16-115 (1988)
New York:	N.Y. JUD. LAW § 497 (McKinney 1988); N.Y. STATE FIN. § 97-v (McKinney 1984)
North Carolina:	North Carolina Rules of Professional Conduct, Rule 10.3 (1988)
North Dakota:	North Dakota Rules of Professional Conduct, Rule 1.15 (1987)
Ohio:	OHIO REV. CODE ANN. § 4705.09 and § 4705.10 (1985)
Oklahoma:	Oklahoma Rules of Professional Conduct, Rule 1.15 (1983)
Oregon:	Oregon Code of Professional Responsibility, DR 9-101(D) (1989)
Pennsylvania:	Pennsylvania Rules of Professional Conduct, Rule 1.15 (1996)
Rhode Island:	Rhode Island Rules of Professional Conduct, Rule 1.15 (1988)
South Carolina:	South Carolina Appellate Court Rules, Rule 412 (1987)
South Dakota:	South Dakota Rules of Professional Conduct, Rule 1.15 (1987)

Tennessee:	Tennessee Code of Professional Responsibility, DR 9-102 (1984)
Texas:	State Bar of Texas Rules, Article XI (1982)
Utah:	Utah Rules of Professional Conduct, Rule 1.15 (1983)
Vermont:	Vermont Code of Professional Responsibility, DR 9-103 (1990)
Virginia:	Rules of the Virginia Supreme Court, Cannon 9, Paragraph 20 of Part 6, § IV (1995)
Washington:	Washington Rules of Professional Conduct, Rule 1.14 (1984)
West Virginia:	West Virginia Rules of Professional Conduct, Rule 1.15 (1989)
Wisconsin:	Wisconsin Supreme Court Rules, Rule 20:1.15 (1989)
Wyoming:	Wyoming Rules of Professional Conduct for Attorneys at Law, Rule 1.15 (1990)